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TAGS: ETRD EAGR EINV RP
SUBJECT: MINDANAO BANANA PROFITS SLIP

SUMMARY

¶1. U.S. banana growers in Davao City reported that profits fell by as much as 40 percent in 2005. They attribute the decline to overproduction, along with increasing operation costs. The Philippines supplies over 95 percent of the total Asian banana market, with exports going primarily to Japan, Korea and the Middle East. U.S. companies Del Monte Fresh, Marsman-Drysdale, and Dole/Stanfilco Philippines produce over half of the total industry and reported combined gross revenues of $322 million for 2005. The three companies alone directly employ over 16,000 people in Mindanao, and contract services employ at least another 20,000 there. Declining profits and possible competition, particularly from India, raise concerns about long-term growth prospects. The industry is backing off from expansion plans. Even so, these "banana powerhouses" are developing strategies to diversify while maintaining their market advantage.

REGIONAL BANANA PRICES PLUMMET

¶2. Meetings with three leading U.S. banana exporters on February 23 and 24 in Davao City revealed that the typically profitable banana export business brought net profit losses for most major U.S. producers in 2005, a trend that is expected to continue in 2006. One company reported as much as a 40 percent decline in net profits in 2005, compared to 2004, which it attributed to a 15 percent increase in fuel costs, a 15 percent increase in salary costs, and increasing contract costs due to the strong peso. In addition, a record number of banana producers resulted in overproduction and market flooding, which caused prices to collapse. Ten years ago, there were about five or six producers, which grew to between ten and twelve in 2005. In Japan, which is the most profitable export market for most U.S. companies, bananas can sell for anywhere between about $5.00 and $12.00 a box, depending on the season, with an average sale price of about $7.00 a box. Companies reported that prices in Japan fell to as little as $1.50 a box in 2005.

PHILIPPINES IS ASIA'S BANANA PLANTATION

¶3. U.S. companies produced well over half the industry total of 164 million boxes of bananas exported in 2005. Del Monte Fresh, Marsman Drysdale, and Dole/Stanfilco reported combined 2005 gross revenues of $322 million. The Philippines supplies over 95 percent of total banana imports

to other countries in Asia, and the vast majority of these bananas are grown in Mindanao. Primary export markets are Japan, Korea and the Middle East. Thailand, Taiwan, and Malaysia produce some bananas, but offer little competition. India has the potential to compete heavily, particularly for the Middle Eastern market due to its proximity, but so far is producing for domestic consumption only. U.S. companies said that if India wanted to start exporting, it could do so "in a heartbeat." Del Monte Fresh and Marsman Drysdale are particularly concerned about India since they export 40 percent and 60 percent of their bananas, respectively, to the Middle East. However, Dole/Stanfilco said that while India has the plantations in place, Indian growers would have to improve their quality to export.

¶4. All three companies grow other fresh produce such as mangoes, pineapples, and asparagus, together less than five percent of total production for Marsman Drysdale and Dole/Stanfilco and about 20 percent for Del Monte Fresh. The majority of pineapple production is handled by sister companies that produce juices and canned fruits, which are among the top three Philippine agricultural exports.

FRUITS OF LABOR

¶5. The three companies employ a combined total of over 16,000 people on Mindanao Island, including a small number of casual laborers during peak seasons. Dole/Stanfilco reported an additional 20,000 employed through contract services. Companies did not report any major labor issues. Dole/Stanfilco added that employment opportunities have brought visible improvements to the quality of life for many people. Many of Dole's plantations are surrounded by

"bandits," but Dole said that the company's employment opportunities are recognized as benefits for the surrounding community and mitigate any potential security problems.

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LAND OWNERSHIP DISPUTES HAMPER BANANA BUSINESS
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¶6. The biggest investment challenge facing U.S. banana growers is land ownership. Some properties may have two or three different titles or no title at all. In addition, land is often owned in small acreage, necessitating a "piecemeal" acquisition strategy. Since U.S. companies cannot own land, they sign long-term lease agreements. Most companies lease and operate about half their production land and then subcontract with individual growers for the balance. Dole/Stanfilco reported a case that has been ongoing for more than five years. The company has a lease agreement for 90 hectares of land, but the ownership is heavily disputed. Dole's position is that it does not matter to them who owns the land. They just need the issue resolved so they can resume production. The 90 hectares can produce about 2.7 million boxes of bananas, or about 8 percent of total 2005 production, which they have omitted from company projections. Dole has been talking to the Department of Agrarian Reform, but has seen no result yet.

SOME GROWERS PEEL BACK INVESTMENT

¶7. Given the poor performance of banana sales in 2005, most companies do not have any immediate plans for additional investment. Dole/Stanfilco said that the company had a three-year investment plan in place, but 2005 results brought investment to a halt. However, Del Monte Fresh is proceeding with expansion plans to develop 800 hectares for pineapple production and 2,200 hectares for banana production. Total investment is valued at $3 million. Del

Monte's representative said that the investment decision was made at corporate headquarters, but may not be well advised given market conditions.

COMMENT

¶8. The banana industry provides a significant number of jobs on Mindanao. Declining profits could result in job losses, which could in turn affect economic stability in Mindanao. U.S. companies are disappointed with 2005 financial results, but these companies are some of the biggest players in the market and are best situated to weather challenging economic conditions. Despite the general pessimism, U.S. companies are developing strategies to maintain their market edge, including expanding more into the Middle East market, devoting more resources to other produce such as pineapples and mangoes, developing organic products to fit niche markets, and competing on the basis of quality. These companies have been in the banana production business in Mindanao for over 20 years, and it is unlikely that a few bad years will have much of an effect on their long-term profitability. However, potential competition from Indian growers could present a more difficult challenge to Philippines-based U.S. companies, forcing them to reevaluate market and production strategies.

KENNEY